This record is a partial extract of the original cable. The full text of the original cable is not available.

C O N F I D E N T I A L SECTION 01 OF 02 PARIS 001312

SIPDIS

STATE ALSO FOR E, EUR/WE, EUR/ERA and EB/OIA
Treasury for Office of International Investment
STATE PASS USTR

E.O. 12958: N/A
TAGS: EINV ETRD ECON PREL FR
SUBJECT: VILLEPIN ECONOMIC ADVISOR ON FRENCH RELATIONS WITH BRUSSELS AND BERLIN, FOREIGN INVESTMENT CLIMATE, EMPLOYMENT

Refs: (A) Paris 1129
(B) Paris 357
(C) Paris 755

Classified by Econ M/C Thomas J White, reasons 1.4 b & d

SUMMARY

¶1. (C) Prime Minister de Villepin's cabinet economic advisor privately describes French-EU relations as being at "an all-time low" on economic issues and worries that the GOF has been unable to find much "traction" with the new German government of Angela Merkel. The advisor defended the openness of France's foreign investment market, citing strong 2005 inbound investment figures, despite continuing evidence of French investment protectionism. Employment remains among the highest priorities of the Villepin government and is a primary driver of Matignon decision-making. END SUMMARY.

INVESTMENT PROTECTIONISM ?
--- -

¶2. (SBU) ECMIN met February 28 with Alain Demarolle, economic advisor in the cabinet of Prime Minister Dominique de Villepin. Demarolle joined Villepin's staff last summer after a number of years on Wall Street. Following a hectic 72 hours February 23-25, Demarolle was flush with the "success" of the proposed merger of parastatal Gaz de France (GDF) with French/Belgian energy and water specialist Suez. The merger -- a marriage hastily arranged through the direct intervention of the Prime Minister's office -- was a forceful and immediate response to an expected hostile takeover bid for Suez by Italian energy giant ENEL. The move has outraged the Italian government, raised concerns at the European Commission in Brussels, and led to extensive international press commentary on emerging French protectionism in the investment sector. Prime Minister de Villepin defended the GDF-Suez merger as essential to French energy security, thwarting what is widely seen as the need for greater European energy sector consolidation and integration.

¶3. (C) Demarolle rejected assertions that the GDF-Suez "marriage' was protectionist. He criticized the Italian government, which holds 30 percent of ENEL, for failing to initiate a dialogue with the GOF in advance of public airing of ENEL's takeover interests. Demarolle asserted that all hostile takeovers will be viewed, at least initially, with suspicion, and expressed a preference for dialogue and consultation on proposed mergers. He admitted that job concerns were a major factor in the Prime Minister's activist response to the takeover rumors, while he was also at pains to portray this as a necessary step in maintaining France's energy security.

¶4. (SBU) Demarolle argued that the French investment climate is much more positive and open than recent media headlines would suggest. Preliminary data for 2005 indicates that both inward and outward investment flows doubled when compared to 2004 results (reftel A). Recent GOF moves to alter foreign investment laws and regulations are designed to address potential problem cases, without altering France's generally open investment regime. Demarolle several times drew comparisons between recent French changes and existing systems and procedures regarding foreign investment in the United States.

¶5. (SBU) ECMIN outlined for Demarolle several USG concerns over the recent strategic investment decree (reftel B):

-- the appearance that the decree may have more to do with preserving existing French jobs than with protecting French national security;
-- apparent preferential treatment for outside investors from EU countries, potentially inconsistent with the 1959 U.S.-France Convention on Establishment, and
-- required prior approval for any investment in any company with headquarters in France, which goes well beyond the "strategic sector" rationale for the decree.

Demarolle argued that the new French decree falls well short of the CFIUS procedures set up under Exon-Florio legislation in the U.S. He admitted, however, that there is concern about expected European Commission examination of the decree in Brussels. On proposed legislation to implement the EU takeover directive, which would permit French firms to mount "poison pill" defenses in hostile takeover cases, Demarolle claimed that the new French proposal was closely copied from existing U.S. practices, and a measure to aid firms facing hostile bids, not a barrier to foreign investment per se.

RELATIONS WITH BRUSSELS AND BERLIN
--- --------------

¶6. (C) France's relations with the European Commission are at a historic "low point," according to Demarolle. He rattled off a litany of recent problem areas: the failed European Constitutional referendum last spring, a bruising EU budget battle, differences over agricultural trade in the WTO talks, criticism of French budget deficits, the Bolkestein services directive, France's failure to secure a value-added tax reduction for restaurants, and now foreign investment policy. Among Commission members, according to Demarolle, only Commission President Barroso and Trade Commissioner Peter Mandelson are viewed with much respect in Paris, and differences with Mandelson on agriculture are well-known.

¶7. (C) Demarolle described worries in the Elysee Palace and Matignon over French-German strategic dialogue and cooperation. The GOF has so far been able to get little "traction" with the new Merkel government, and the current dialogue falls short of the close dialogue with the previous Schroeder government.

EMPLOYMENT -- JOB ONE

¶8. (C) Spurred by deep-seated French public fears of globalization, outsourcing and corporate downsizing, Prime Minister de Villepin has demonstrated consistently strong instincts to protect existing French jobs. Last summer's flap over a rumored Pepsi takeover of Danone, strong criticism of Hewlitt-Packard's global cost-cutting efforts last fall, expressed suspicion of Mittal Steel's proposed purchase of Luxembourg-based Arcelor (ref C), and the Gaz de France-Suez merger are all examples of a "save jobs first" mentality. Demarolle admitted that the Prime Minister sees employment as a major litmus test of his political success, and a major barometer of his political future.

COMMENT

¶9. (C) Most French politicians recognize the importance of foreign investment, and are quick to applaud the efforts of French firms to expand abroad. However, France's strong attachment to its social model, and fears of globalization and outsourcing, make most French officials reflexively defensive in responding to possible foreign takeovers of French firms. For the moment, "It's the job market - stupid!" seems to be the ruling mantra, and will likely color most economic decision-making through the 2007 elections.

STAPLETON